

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING #97-56**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

The accounting period to be covered by the Tennessee franchise, excise tax return that the Taxpayer will file after selling substantially all of its assets and the proper calculation of franchise, excise taxes on such return.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the Department by the Taxpayer. The rulings herein are binding upon the Department, and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time. Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The Taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (C) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The Taxpayer directly involved must have acted in good faith in relying upon the ruling and a retroactive revocation of the ruling must inure to his detriment.

FACTS

The Taxpayer is a Delaware corporation with a fiscal year ending the last Saturday in September. It will be filing a federal tax return with the Internal Revenue Service to cover the tax year beginning September 29, 1996 and ending September 27, 1997. On [DATE OF SALE DURING TAX YEAR], the Taxpayer sold substantially all of its business assets

and ceased all business activities in Tennessee. Since that time, the Taxpayer has had no property, payroll or sales in Tennessee.

The Taxpayer liquidated its manufacturing operations everywhere on [DATE OF SALE] but because of the need to make disposition of certain relatively minor assets, the need to make disposition of certain lawsuits and an employee stock ownership plan, and the need to do certain acts pursuant to the liquidation, such as give notice to its creditors, the Taxpayer continues to exist.

The Taxpayer's only remaining activity is that of making an orderly disposition of what remains of its business after the [DATE OF SALE] sale. This is being conducted from [STATE A - NOT TENNESSEE] and was not be completed by its September 27, 1997 year end. Although the Taxpayer has ceased all business activities in Tennessee, it can not formally withdraw from Tennessee until all franchise, excise tax returns are filed and the taxes due thereon are paid.

ISSUES

1. What time period should the Taxpayer's current year Tennessee franchise, excise tax return cover?
2. How should the Taxpayer calculate its franchise, excise taxes on such return?

RULINGS

1. The Taxpayer's current year franchise, excise tax return should cover the tax year beginning September 29, 1996 and ending September 27, 1997.
2. For franchise, excise tax purposes, the Taxpayer will compute an apportionment formula for the tax year based on property, payroll and sales. Property to be included in the apportionment formula should be averaged pursuant to TENN. COMP. R. & REGS. 1320-6-1-.29. Pursuant to TENN. COMP. R. & REGS. 1320-6-1-.11(2), balance sheet values immediately prior to the [DATE OF SALE] sale will be used in computing net worth for franchise tax purposes and property included in the franchise tax minimum measure. The excise tax rate will be applied to net earnings computed pursuant to T.C.A. § 67-4-805 and apportioned to Tennessee. Neither the franchise tax nor the excise tax may be prorated.

ANALYSIS

1. **FRANCHISE, EXCISE TAX RETURNS MUST BE FILED
TO COINCIDE WITH FEDERAL RETURNS**

TENN. COMP. R. & REGS. 1320-6-1-.02(2) provides that a franchise, excise tax return must be filed “. . . to coincide with each accounting period for which a federal return has been filed.” In *DACCO, Inc. v. Huddleston*, 891 S.W.2d 920 (Tenn. App. 1994), permission to appeal denied by the Tennessee Supreme Court January 30, 1995, the Tennessee Court of Appeals, Middle Section, upheld this Rule.

Accordingly, the Taxpayer's current franchise, excise tax return must be filed to coincide with the accounting period covered by its federal return which covered the tax year beginning September 29, 1996 and ending September 27, 1997.

2. CALCULATION OF FRANCHISE, EXCISE TAXES FOR THE TAX YEAR
BEGINNING SEPTEMBER 29, 1996 AND ENDING SEPTEMBER 27, 1997

T.C.A. §§ 67-4-910 and 67-4-811 require the Taxpayer to compute the standard property, payroll and receipts apportionment formula. As a result of the [DATE OF SALE] sale of assets, property values fluctuate considerably from the beginning to the end of the tax year. Therefore, for purposes of the property factor of the apportionment formula, such values should be averaged in accordance with TENN. COMP. R. & REGS. 1320-6-1-.29(2) set forth below.

- (2) Averaging by monthly values will generally be applied if substantial fluctuations in the values of the property exists during the tax period or where property is acquired after the beginning of the tax period or disposed of before the end of the tax period.

Example: The monthly value of the taxpayer's property was as follows:

January	\$ 2,000
February	2,000
March	3,000
April	3,500
May	4,500
June	<u>10,000</u>
	\$25,000
July	15,000
August	17,000
September	23,000
October	25,000
November	13,000
December	<u>2,000</u>
	\$95,000
 TOTAL	 \$120,000

The average value of the taxpayer's property includable in the property factor for the income year is determined as follows:

$$\$120,000 \div 12 = \$10,000$$

Averaging with respect to rented property is achieved automatically by the method of determining the net annual rental rate of such property as set forth in Rule 1320-6-1-.28(b).

For purposes of the property factor of the franchise, excise tax apportionment formula, the Taxpayer's property should be valued at its original cost basis for federal income tax purposes (prior to any federal adjustments) at the time of acquisition. TENN. COMP. R. & REGS. 1320-6-1-.28.

Payroll and receipts for the entire accounting period should be included in the apportionment formula's payroll and receipts factors in accordance with T.C.A. §§ 67-4-811 and 67-4-910.

TENN. COMP. R. & REGS. 1320-6-1-.11(2) makes the following provisions concerning the computation of the franchise tax base of a corporation that has liquidated.

(2) ...The franchise tax will be determined by using the closing near date of surrender, withdrawal or a closing associated with or immediately preceding merger, liquidation or consolidation. In all cases corporations must submit a schedule of liquidation, distribution or disposition of all assets.

The Taxpayer effectively liquidated its business on [DATE OF SALE]. Pursuant to T.C.A. §§ 67-4-904, 67-4-906 and TENN. COMP. R. & REGS. 1320-6-1-.11(2), balance sheet book values immediately prior to the [DATE OF SALE] liquidation should be used to compute net worth for franchise tax purposes and real or tangible personal property and rental values of property used for purposes of the franchise tax minimum measure. Book values used for these purposes should be at cost less accumulated depreciation and in accordance with Generally Accepted Accounting Principles. Net worth so computed will be apportioned using the apportionment formula described above and the franchise tax rate will be applied to the greater of apportioned net worth or the book value of Tennessee real or tangible personal property owned or used. The franchise tax so computed is not subject to proration under TENN. COMP. R. & REGS. 1320-6-1-.05 because no short period return is involved.

This is consistent with the Department's long standing application of TENN. COMP. R. & REGS. 1320-6-1-.11(2) in factual situations similar to those described by the Taxpayer.

The Taxpayer's excise tax will be computed by applying the tax rate to the corporation's apportioned net earnings computed in accordance with T.C.A. § 67-4-805 for the entire year. Computation of the apportionment formula to be used has already been discussed. Neither the Tennessee law nor the Rules of the Department or Revenue make any provision for proration of the excise tax in any case.

Until it formally withdraws its Tennessee Certificate of Authority, the Taxpayer will continue to file Tennessee franchise, excise tax returns to cover each accounting period after the tax year ended September 27, 1997. However, as long as the Taxpayer is completely inactive in Tennessee during each subsequent tax year and owns or rents no

property here, only the \$10.00 minimum franchise tax will be due on each return filed for future periods. See T.C.A. § 67-4-907.

Arnold B. Clapp, Senior Tax Counsel

APPROVED: _____
Ruth E. Johnson, Commissioner

DATE: 12-22-97